

1 **Lack of effective competition in the New Jersey local service market**
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3 26. While various Verizon NJ declarants offer testimony purporting to demonstrate that
4 Verizon NJ has fully complied with all of the fourteen requirements set forth in the Section
5 271(c)(2)(B) "competitive checklist," the minimal level of competitive penetration that
6 presently exists in New Jersey, even taking Mr. Bone's figures at their face value, belies those
7 contentions. If the local service market were "irreversibly opened to competition" as Verizon
8 NJ contends, CLECs would be flocking to New Jersey — one of the most lucrative telecom-
9 munications markets in the nation — rather than running from it. There is thus no basis upon
10 which the Board may reasonably determine that all competitors have fair, nondiscriminatory,
11 and mutually open access to exchanges currently subject to the modified final judgment and
12 interexchange facilities, including fair unbundling of exchange facilities.

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14 27. Significantly, the level of residential CLEC market penetration in New Jersey is one
15 of the lowest in the entire country. Mr. Bone has identified some 59,000 residential lines
16 being provided by CLECs via resale of bundled VNJ services, and another 280 that he
17 portrays as "facilities-based." Taken together, both groups of CLEC customers account for
18 only 1.35% of the 4.34-million residential access lines that are currently being served *at retail*
19 by Verizon New Jersey. Indeed, the "facilities-based competition" in the residential market
20 — the existence of which must be affirmatively demonstrated as a specific precondition for
21 Section 271 authority as required at Section 271(c)(1)(A) of the federal Act — accounts for
22 only 0.0065% of the total residential access line market in Verizon NJ's service territory.
23 Moreover, inasmuch as this figure of 280 was apparently gleaned by Verizon NJ from its

1 E911 database (which identifies a customer as being served by a CLEC when the CLEC
2 furnishes the switching facilities), there is no showing that any of these 280 residential lines
3 utilize CLEC-provided *outside plant facilities* rather than UNE-loops obtained from Verizon
4 NJ and resold as part of the CLEC retail service. Hence, Verizon NJ has failed to demon-
5 strate, as it is required to do, that “such [facilities-based] telephone exchange service may be
6 offered by such competing providers either exclusively over their own telephone exchange
7 service facilities or *predominantly over their own telephone exchange service facilities* in
8 combination with the resale of the telecommunications services of another carrier.”⁴⁰ The
9 absence of verification of a competing facilities-based provider of residential service is by
10 itself fatal to the Verizon New Jersey Section 271 application, and is by itself a basis for that
11 application to be denied.⁴¹

12

13 28. When state commissions expend the time and effort necessary to develop a record
14 such as the FCC recommends, the FCC has consistently given more weight and consideration
15 to the state commission recommendations.⁴² Indeed, the Board's consultative role

16 40. 47 CFR 271(c)(1)(A), emphasis supplied.

17 41. The FCC appears to have determined that a CLEC's use of UNEs constitutes
18 “facilities-based” competition. Even if, in fact, these 280 “facilities-based” plus 400 UNE-P
19 CLEC residential lines are being furnished “by such competing providers ... exclusively over
20 their own telephone exchange service facilities,” the infinitesimal fraction of the total New
21 Jersey residential access line market that this one (or more) CLEC(s) would be serving hardly
22 demonstrates the existence of an “irreversible” competitive presence. It defies reason to
23 imagine that even one firm — let alone more than one — could survive very long with so
24 minute a customer and revenue base in this market segment.

25 42. *Texas 271 Order*, at para 11.

1 unambiguously embraces Section 271(c)(1)(A) and thus *requires* that the Board examine the
2 status of competition in New Jersey and make a finding as to the presence of a facilities
3 based residential and business provider. Moreover, although Section 271(c)(1)(A) requires
4 that VNJ demonstrate the presence of at least one facilities-based provider in each of the
5 residential and business segments — which Verizon NJ has not complied with in its filing —
6 this nominal test for the presence of local competition must be read in the broader context of
7 the Section 271(d)(3)(C) “public interest” requirement: Clearly, the purpose of requiring the
8 presence of local competition as a prerequisite to interLATA entry was to assure that the
9 incumbent BOC would not be capable of using its local market dominance to remonopolize
10 the adjacent long distance market. In the instant matter, the claimed existence of only 280
11 residential subscribers that, according to VNJ, are ostensibly being served in some unspecified
12 manner by a facilities-based carrier in unspecified geographic areas, cannot possibly offer any
13 assurance that VNJ’s market power is in any material sense attenuated by the existence of
14 competition or that VNJ would be unable to leverage its control of in excess of 99.99% of the
15 New Jersey facilities-based residential service market to regain effective monopoly control of
16 the in-region long distance market with respect to this major customer segment.

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18 29. As I have previously explained, the notion underlying Section 271 of the 1996
19 federal *Act* is that once the local exchange market becomes competitive such that consumers
20 have a real choice with respect to local service provider, no one local service provider will
21 possess a monopoly in this segment and thus be capable of leveraging that monopoly to
22 similarly monopolize and dominate the adjacent long distance market. Consequently, in its

1 September 5, 2001 Section 271 filing with this Board, Verizon NJ undertakes, through the
2 declaration of Dennis Bone, President of Verizon NJ, to demonstrate the presence of
3 significant competition in the New Jersey local service market. Mr. Bone claims that Verizon
4 NJ is currently operating in a market where CLECs are positioned to serve most if not all
5 existing customers. Were that the case — which as I shall show it clearly is not — Verizon
6 NJ could presumably claim that its service area was significantly and irreversibly opened to
7 competition. The validity of Mr. Bone's methods for determining levels of competition and
8 CLEC competitive potential is therefore integral to this proceeding. As I shall demonstrate,
9 the various claims and assertions advanced by Mr. Bone serve only to confirm Verizon NJ's
10 current, ongoing and overwhelming dominance of the New Jersey local service market, and in
11 that regard his testimony fails to make a showing regarding the sustainable presence of local
12 competition for the reasons I discuss below.

13

14 30. Given the immense amount of capital that has been invested by firms seeking to
15 enter the New Jersey local services market and the effort that has been expended by these
16 firms to pursue that goal, if Verizon NJ had truly "opened its network" to competitive access
17 and entry, we should be observing far more competitive activity than even Mr. Bone's
18 exaggerated account seeks to portray. Indeed, even Mr. Bone concedes that Verizon NJ's
19 share of the local service market in its operating areas in New Jersey may be as high as
20 93.3%,⁴³ and asks the Board to accept the idea that a mere 6.7% level of competitive pene-
21 tration after more than five and a half years following enactment of the 1996 Act constitutes

22 43. Bone (Verizon NJ), Declaration at 7.

1 an effectively competitive market. If Verizon NJ's network were truly open and accessible to
2 CLECs, the competitive nature of the local service market in New Jersey would not even be a
3 matter of dispute or debate. Mr. Bone himself thus provides compelling evidence that
4 competitors do *not* have fair, nondiscriminatory, and open access to Verizon NJ exchanges
5 and network facilities.

6
7 31. The most clear and direct way to measure a CLEC's market penetration is to count
8 the access lines that it is actually serving. An "access line" for this purpose is a physical
9 voice-grade equivalent facility providing dial tone to an end user customer. In fact, Verizon
10 NJ has offered no evidence of the actual number of access lines currently being furnished by
11 facilities-based CLECs and has thus resorted to various types of "shadow" evidence that Mr.
12 Bone undertakes to "interpret" as conveying far more market intelligence than it actually
13 does.

14
15 32. One such "shadow" approach that Verizon NJ has employed is to extract certain
16 information from the carrier E911 database that Verizon NJ is responsible for managing,⁴⁴

17 44. In this regard and as an aside, Verizon NJ's use of the carrier E911 data base to extract
18 market information is in itself evidence of an abuse of its monopoly position. Apparently,
19 Verizon is able to obtain extremely granular market data about its competitors' activities from
20 this data source that it exclusively controls. By mining the E911 database and assuming that
21 it is sufficiently accurate for the conclusions being drawn by Mr. Bone to be valid, Verizon
22 apparently can identify the quantity of access lines being provided by each of its CLEC
23 competitors in each exchange area — the type of information that Verizon characterizes as
24 "CLEC proprietary data" in both its prefiled evidence as well as in responses to data requests.
25 While this information is not being furnished to Verizon's competitors or the Ratepayer

(continued...)

1 and to integrate those results with other “shadow” data to which Verizon NJ has access, such
2 as the number, location, and carrier for interconnection trunks and collocation arrangements.
3 Through discovery, however, it is apparent that each of Mr. Bone’s methods involve
4 assumptions or distortions that seriously inflate this important competitive indicator.

5
6 33. Mr. Bone initially portrays the E911 database as a “conservative” source of CLEC
7 access line counts. By summing all numbers entered in the database identified by CLEC
8 NXX codes, and then adding the number of UNE-P access lines, Mr. Bone claims to present
9 what he characterizes as a “highly conservative calculation” of CLEC facilities-based lines.⁴⁵
10 When queried in discovery, however, it becomes clear that Mr. Bone made no attempt to
11 determine the actual occurrence of any theory that would justify characterizing this estimate
12 as “conservative,” much less “highly conservative.” Mr. Bone could produce no practices
13 manual or other documentation detailing CLEC procedures for entering information into the
14 E911 database.⁴⁶ More importantly, however, while Mr. Bone contends that the E911

15 44. (...continued)
16 Advocate, Verizon is apparently making liberal use of the very same “CLEC proprietary”
17 market data for its own competitive and strategic purposes, such as its use in this proceeding
18 to buttress its efforts to obtain Section 271 authority. Inasmuch as Verizon does not make this
19 information available to its competitors nor the Ratepayer Advocate while at the same time
20 utilizing it for its own purposes, the practice is on its face competitively unfair, and likely
21 violates the express prohibition, set out at Section 222(b) of the federal Act, that “[a]
22 telecommunications carrier that receives or obtains proprietary information from another
23 carrier for purposes of providing any telecommunications service shall use such information
24 only for such purpose, and shall not use such information for its own marketing efforts.”

25 45. Bone (Verizon NJ), Declaration, attachment 101, at 3.

26 46. Verizon NJ Response to RPA-26.d.

1 database is a listing of access lines,⁴⁷ in fact Verizon New Jersey's own E911 database
2 entries exceed its access line count by nearly 450,000.⁴⁸ In response to a Ratepayer
3 Advocate data request, Mr. Bone states that he made no attempt to explain or account for
4 CLEC practices with respect to the treatment of Direct Inward Dialing (DID) numbers
5 assigned to customers, which would typically exceed the actual number of access lines that
6 the customer obtains from a CLEC.⁴⁹ Contrary to Mr. Bone's speculation, the quantity of
7 CLEC-associated numbers in the E911 database could well be significantly greater than the
8 actual number of CLEC access lines in service.⁵⁰ If in fact the "CLEC E911 number

9 47. Verizon NJ Response to RPA-26.b.

10 48. See Verizon NJ Response to RPA-26.c. Verizon NJ gives the number of its
11 customers' E911 entries at 7,186,000, yet its total access lines are given as only 6,740,457.
12 Bone (Verizon NJ), Declaration, at para. 7, footnote 4.

13 49. Verizon NJ Response to RPA-26.d.

14 50. This is due to common business communications arrangements such as DID, where
15 each station line "behind" a PBX is assigned its own unique 7-digit telephone number. A
16 DID customer will obtain a block of numbers from its local carrier, ILEC or CLEC, and that
17 quantity of individual numbers will typically be a multiple of the quantity of physical access
18 lines (PBX trunks) that are being provided to that customer. For example, FCC rules relating
19 to surcharges for Local Number Portability ("LNP") allow an ILEC to apply nine (9) LNP
20 charges for each PBX trunk or equivalent; thus, in the case of a T-1 trunk containing 24
21 individual voice channels, the FCC LNP rules contemplate 24 x 9, or 216 PBX stations
22 "behind" the single T-1 facility. 47 CFR Part 52, subpart 33(i). Although carriers do not
23 necessarily report all DID numbers to the E911 data base, their individual practices in this
24 regard are not uniform and, in any event, are not known and were not even researched by Mr.
25 Bone or by Verizon NJ. Verizon NJ Response to RPA-26.d. DID numbers would require
26 E911 presence if the customer's PBX was capable of identifying the calling station line on
27 outgoing calls. While this "Identified Outward Dialing" ("IOD") capability is by no means
28 universally present, the CLEC has no consistent means of determining the capabilities of
29 individual customers' PBXs and, in an abundance of caution, may include all of the numbers
30 (continued...)

1 counts" that Mr. Bone interprets as CLEC *access lines* include DID numbers, the CLEC
2 market share figures that he presents based thereon would be seriously exaggerated.
3 Moreover, a CLEC will typically include its own customer in the E911 database where the
4 CLEC provides the *switch*, even if Verizon is the underlying provider of the access line
5 facility connecting the customer's premises with the CLEC switch. Hence, when combined
6 with the lack of correspondence between E911 listings and CLEC customer access lines, the
7 E911 database count is not a reliable indicator of the amount of CLEC-provided facilities in
8 the New Jersey market.

9
10 34. Another "shadow" approach that Mr. Bone uses to estimate CLEC competitive
11 potential is to offer the number of completed collocation arrangements as an indicator of both
12 the existence of and potential for facilities-based competition.⁵¹ Mr. Bone cites 1,000
13 collocations in VNJ wire centers,⁵² and thus asserts that a significant number of CLECs are
14 positioned to directly compete with Verizon NJ.⁵³ The strength of potential competition,
15 however, is mitigated significantly when the number of failing CLECs is considered.

16 50. (...continued)
17 in the DID number block in the E911 entry for that customer. Pending FCC rules would
18 require PBXs to have the IOD capability for E911 purposes at least with respect to a limited
19 number of PBX station lines. *In the Matter of Revision of the Board's Rules to Ensure*
20 *Compatibility with Enhanced 911 Emergency Calling Systems*, CC Docket 94-102, 9 FCC Rcd
21 6181, at para. 60.

22 51. Bone (Verizon NJ), Declaration at para. 6.

23 52. *Id.*

24 53. *Id.*

1 According to Verizon NJ's own records, a full 232 collocations — more than 23% of the total
2 cited by Mr. Bone — currently have a payment due to Verizon NJ for the collocation space
3 that is more than 30 days past due.⁵⁴ Additionally, Verizon NJ has also admitted that it has
4 received discontinuation orders for 391 existing collocation arrangements.⁵⁵ Thus, as none
5 of the discontinuation orders are currently past due,⁵⁶ fully 62% of the 1,000 current
6 collocation arrangements that Mr. Bone claims to exist pose no serious competitive threat to
7 Verizon NJ, since they are unlikely to have a long-term potential for survival. Again,
8 Verizon's support for purported local competition in New Jersey falls short.

9
10 35. Moreover, some (albeit an unspecified number) of the collocation arrangements cited
11 by Mr. Bone are undoubtedly associated with "data CLECs," i.e., carriers providing Digital
12 Subscriber Line (DSL) services. As has been demonstrated with respect to CLEC entry into
13 the local voice telephone service market, entry into these other service areas is also proving to
14 be expensive, due to high fixed costs associated with acquiring the necessary facilities. A
15 compelling demonstration of the prevailing dearth of confidence in the data CLECs' ability to
16 successfully develop their networks and even to expand into voice-over-IP service can be seen
17 in the decision last year by Verizon to pull out of its plans to acquire a 55% stake in
18 NorthPoint Communications. Following this decision, a Verizon spokesperson claimed that
19 the Company had "several other ways" of gaining customers in the DSL markets outside of

20 54. Verizon NJ Response to RPA-27.a.i.

21 55. Verizon NJ Response to RPA-27.a.iii.

22 56. Verizon NJ Response to RPA-27.a.iv.

1 Verizon's traditional territory.⁵⁷ In March 2001, AT&T acquired the *physical assets* of
2 NorthPoint for about \$135-million, less than 10% of the pre-Verizon-merger market value of
3 NorthPoint as a going concern, and only about "25 cents on the dollar" ... for NorthPoint's
4 'hard assets.'"⁵⁸ In fact, certain data CLECs, such as Covad and Rhythms NetConnections,
5 are already operating under Chapter 11 protection.⁵⁹

6

7 36. A June 18, 2001 *New York Times* analysis of the fiber optic long-haul "backbone"
8 market underscores the utter lack of competition at the *local* distribution end of the
9 information superhighway:

10

11 There is a glut of capacity of high-speed, long-haul information pipelines, but a
12 shortage of the high-speed local-access connections that consumers and
13 businesses need to connect to the Web. It is as if superhighways stand nearly
14 empty while traffic backs up at the Holland and Lincoln tunnels.

15

16 Few people have fast Internet connections, and prices are rising for those who
17 do. ...⁶⁰

18

19 Ironically, while the demand for bandwidth is clearly present and growing, the ILEC-
20 controlled local access monopoly is working effectively to block that demand from ever

21 57. "Citing Declining Operations, Financial Results, Verizon Backs Away From Takeover
22 Of NorthPoint," *TR Daily*, November 29, 2000.

23 58. *Telecommunications Reports*, March 26, 2001; *TR's Last-Mile Telecom Report*, August
24 8, 2000.

25 59. *TR Daily*, August 2, 2001; August 15, 2001.

26 60. "Once-Bright Future of Optical Fiber Dims," *New York Times*, June 18, 2001, p. A1.

1 reaching the overabundant supply. Given the tens of billions of dollars that have been
2 invested in backbone fiber, one would certainly expect that, were realistic competitive
3 opportunities actually available in the local service market, at least some of that investment
4 capital would have been and would even today be deployed in this direction. The fact that
5 the local ILEC bottleneck persists, and that investors are running away from pursuing local
6 service entry as fast as they can, speaks volumes about the actual state of local competition
7 both nationally and more specifically in New Jersey, where demand for Internet access is
8 extremely high.⁶¹

9

10 37. Indeed, one need look no further than the recent actions of SBC and Verizon for
11 confirmation of the extreme difficulties that entrants confront in competing with ILECs in the
12 local services market. SBC, in its Joint Application for approval of its merger with
13 Ameritech,⁶² and Verizon, in its Joint Application for approval of its merger with GTE,⁶³

14 61. One might even go so far as to theorize an affirmative business strategy on the part of
15 SBC, Verizon and the other RBOCs to deliberately withhold the availability of high-speed
16 Internet access so as to enfeeble the backbone fiber optic network providers to the point
17 where, following their attainment of Section 271 authority, the RBOCs will be in a position to
18 purchase those backbone network assets at fire-sale prices.

19 62. *In re: Applications of Ameritech Corp., Transferor, and SBC Communications, Inc.,*
20 *Transferee, for Consent to Transfer Control of Corporations Holding Board Licenses and*
21 *Lines Pursuant to Sections 214 and 310(d) of the Communications Act and Parts 5, 22, 24,*
22 *25, 63, 90, 95, and 101 of the Board's Rules*, CC Docket No. 98-141, ("SBC/Ameritech
23 Merger Application"), at Sec. II.A.1.

24 63. *Applications of GTE Corporation and Bell Atlantic Corporation, Description of the*
25 *Transaction, Public Interest Showing and Related Demonstrations*, CC Docket No. 98-184
26 (October 2, 1998) ("Bell Atlantic/GTE Merger Application"), Declaration of Jeffrey C.
27 Kissell, at para. 14.

1 each represented that following their respective mergers the two mega-ILECs would each
2 commit to pursuing "out-of-region" entry in various local exchange service markets. SBC
3 had identified thirty such markets (of which 12 would be in what would become Verizon
4 territory),⁶⁴ while BA/GTE (Verizon) committed to enter twenty-one markets, of which
5 eleven would be in the expanded 13-state SBC region.⁶⁵ Although various parties and their
6 experts, including myself, expressed serious doubts as to the legitimacy of these so-called
7 "commitments," both sets of joint applicants insisted that their respective "national local
8 strategies" would be aggressively pursued and would result in a significant enhancement of
9 local competition throughout the country.⁶⁶

10

11 38. In its Orders approving the two mergers, the FCC undertook to put some teeth into
12 what were in other respects "soft" commitments on the part of the two sets of merger parties
13 with respect to their out-of-region local entry plans. In its *SBC/Ameritech Order*, the
14 Commission *required* the promised entry, and indicated that the post-merger SBC would be
15 fined as much as \$39.6-million for each of the 30 out-of-region markets that it did not
16 enter.⁶⁷ In the *BA/GTE Order*, the FCC similarly imposed the threat of fines if BA/GTE

17 64. SBC/Ameritech Merger Application, Attachment A: "New Markets for the New SBC"

18 65. Bell Atlantic/GTE Merger Application, Declaration of Jeffrey C. Kissell, at para. 14.

19 66. *Id.*, at para. 15; SBC/Ameritech Application, Affidavit of James S. Kahan, at para. 27.

20 67. SBC/Ameritech Merger Order, FCC 99-279, October 6, 1999, at Appendix C, para.
21 59(d). "If an SBC/Ameritech Out-of-Territory Entity fails to satisfy any of the 36 separate
22 requirements for each out-of-territory market on or before the deadlines set forth in

23

(continued...)

1 failed to invest at least \$500-million in out-of-region CLEC activities, or provide service as a
2 CLEC to at least 250,000 customer lines, by the end of 36 months following the merger
3 closing date.⁶⁸

4

5 39. As it has turned out, of course, the skepticism of various commentators and the
6 concerns of the FCC with respect to the veracity of these out-of-region local entry
7 "commitments" were well-founded. Earlier this year, both SBC and Verizon announced that
8 they had each abandoned or drastically scaled-back their out-of-region local entry plans.⁶⁹

9

10 40. In the five-year period following enactment of TA96, various mergers have been
11 approved among large incumbent LECs that have reduced the number of Regional Bell
12 Operating Companies (plus GTE) from eight to four. At the time that each of these mergers
13 was first announced publicly, these large carriers had in each case promised that their
14 combination would further the pro-competitive purposes of the Act. Based upon the
15 competitive entry data set forth above, it is clear that, both in New Jersey and on a national
16 scale, these mergers have done nothing but create larger, better financed fortress bottleneck

17 67. (...continued)

18 Subparagraph c, SBC/Ameritech shall make a one-time contribution of \$1.1 million for each
19 missed requirement (up to a total contribution of \$39.6 million per market and \$1.188 billion
20 if SBC/Ameritech Out-of-Territory Entities fail to satisfy all 36 requirements in all 30
21 markets) to a fund to provide telecommunications services to underserved areas, groups, or
22 persons."

23 68. *BA/GTE Merger Order*, at paras. 43-48.

24 69. *TR Daily*, January 15, 2001, March 21, 2001.

1 monopolies. Indeed, the RBOCs' resistance to the market opening conditions of the Act has
2 proven so successful that the competitive local exchange carrier industry now stands on the
3 verge of collapse.⁷⁰

4
5 41. Competitive LECs have become marginalized because they do not own the strategic
6 assets necessary to compete, and must instead rely upon the ubiquitous Bell network, a
7 network that remains largely closed to new entrants, Sections 251 and 252 notwithstanding.
8 There has been carnage among CLEC stocks, and numerous competitive LECs have filed or
9 are on the verge of filing for bankruptcy.⁷¹ From a financial perspective, many CLECs
10 operating within New Jersey are experiencing a major economic downturn. The optimistic
11 tone of the Bone declaration would have one believe that CLECs are stronger than they have
12 ever been in their ability to capture market share, when in fact just the opposite is true.
13

14 70. See, e.g., *In the matter of Joint Application of Onepoint Communications Corp. and*
15 *Verizon Communications for Authority Pursuant to Section 214 of the Communications Act of*
16 *1934, as Amended, to Transfer control of Authorizations to Provide Domestic Interstate and*
17 *International Telecommunications Services as a Non-Dominant Carrier*, CC Docket No. 00-
18 170, AT&T's *Petition to Deny Joint Applications*, October 23, 2000.

19 71. As discussed above, NorthPoint filed for bankruptcy on January 16, 2001. Another
20 DSL provider, HarvardNet, pulled out of the DSL market in December 2000. HarvardNet
21 decided to restructure its business to focus on Web hosting, citing the capital intensive nature
22 of the DSL market, as well as the "recent dramatic downturn in the financial markets" as
23 reasons for discontinuing its DSL service. "DSL Providers NorthPoint, HarvardNet Cut Jobs,"
24 *TR Daily*, December 7, 2000. Additionally, and as previously mentioned, Covad and
25 Rhythms have now also filed for Chapter 11 protection.

1 42. The fact that CLECs can expect to encounter substantial difficulty in raising capital
2 is reflected in the recent sharp drop in their overall market capitalizations. This past August
3 (2001), CLEC analysts at Morgan Stanley Dean Witter noted that the market capitalization of
4 CLECs as a group had fallen by 65.8% since January 1, 2001.⁷² This figure does not
5 account for the drop-off in CLEC stock prices that began in the fourth quarter of 2000 and
6 that have continued since the Morgan Stanley report was issued. As illustrated in Table 1
7 below, many of the carriers identified by Mr. Bone have experienced a precipitous drop — in
8 the range of 65% — in stock price and market capitalization over the past 24 months.

9
10 43. As Table 1 confirms, the situation has certainly not improved for CLECs over the
11 past year. The dramatic decreases in CLEC share prices indicate that (1) investors have less
12 confidence in these companies' ability to succeed with business plans premised upon compet-
13 ing with ILECs; and (2) the companies themselves now will have much more difficulty
14 attracting capital with which to pursue their business plans. Telecommunications is an
15 industry requiring a substantial amount of up-front investment, and a lack of capital with
16 which to pursue market entry will surely adversely impact a carrier's ability to gain market

17 72. Morgan Stanley Dean Witter, Equity Research: North America, Industry: Competitive
18 Local Exchange Carriers (CLECs), August 14, 2001, at 1. In an earlier report issued by
19 MSDW, its analysts indicated that "[u]nlike the last two CLEC market corrections, we do not
20 believe that the current one is likely to end with the entire group rocketing back because, over
21 the next six months, we expect news headlines to be peppered with reports of additional
22 bankruptcies." Morgan Stanley Dean Witter, Equity Research: North America, Industry:
23 Competitive Local Exchange Carriers (CLECs), November 7, 2000, at 2.

TABLE 1
CLEC Market Capitalization

Company	September 30, 1999			October 16, 2001			% change from 9/30/99 to 10/16/01
	stock price	In Millions		stock price	In Millions		
		Shares out-standing	Market Cap		Shares out-standing	Market Cap	
Adelphia	\$ 28.00	51.4	\$ 1,439.7	\$ 0.96	134.5	\$ 127.8	-91%
Allegiance	\$ 63.00	64.9	\$ 4,086.5	\$ 5.79	113.7	\$ 727.9	-82%
AT&T Corp	\$ 47.44	3195.6	\$ 151,592.9	\$ 19.20	3530.0	\$ 70,600.0	-53%
Commonwealth Tele	\$ 44.00	22.1	\$ 972.8	\$ 40.94	23.3	\$ 931.0	-4%
Connectiv	\$ 19.63	87.3	\$ 1,712.6	\$ 23.25	88.7	\$ 2,080.0	21%
CoreCom	\$ 37.19	72.1	\$ 2,679.4	\$ 0.08	98.4	\$ 7.8	-100%
CTC Communications	\$ 16.44	14.6	\$ 239.2	\$ 5.58	26.9	\$ 138.5	-42%
CTCI	\$ 47.00	19.9	\$ 936.5	\$ 14.14	18.5	\$ 268.0	-71%
Focal	\$ 23.94	60.6	\$ 1,451.7	\$ 0.59	61.8	\$ 34.0	-98%
Global Crossing	\$ 26.50	794.8	\$ 21,061.4	\$ 1.14	887.3	\$ 7,276.0	-65%
GST Telecomm Inc	\$ 7.03	37.7	\$ 265.2	\$ -		\$ -	-100%
Northpoint	\$ 24.31	125.2	\$ 3,044.9	\$ -		\$ -	-100%
ICG Communications	\$ 15.56	47.3	\$ 736.8	\$ -		\$ -	-100%
Level 3 Communications	\$ 52.22	341.1	\$ 17,810.6	\$ 3.31	368.3	\$ 1,080.0	-94%
Worldcom	\$ 76.88	1880.2	\$ 144,541.8	\$ 14.03	2960.0	\$ 41,000.0	-72%
RCN	\$ 49.69	76.2	\$ 3,785.4	\$ 3.10	97.3	\$ 293.9	-92%
Sprint	\$ 54.25	785.2	\$ 42,597.4	\$ 23.60	973.4	\$ 22,800.0	-46%
Time Warner	\$ 21.38	81.3	\$ 1,736.7	\$ 11.00	114.3	\$ 1,270.0	-27%
Winstar Comm Inc	\$ 39.06	54.9	\$ 2,145.9	\$ -		\$ -	-100%
XO Comm/Nextel	\$ 61.38	315.5	\$ 19,360.8	\$ 0.71	429.8	\$ 275.1	-99%
Total CLEC			\$ 422,198.2			\$ 148,910.0	-65%

Source: carrier 10Q reports, www.thedigest.com/stocks/

TABLE 2
RBOC Market Capitalization

	September 30, 1999			October 16, 2001			
		In Millions			In Millions		
Company	stock price	Shares out-standing	Market Cap	stock price	Shares out-standing	Market Cap	% change from 9/30/99 to 10/16/01
BellSouth	\$ 43.25	1885.0	\$ 81,526.3	\$ 39.40	1,880	\$ 73,800.0	-9%
Ameritech	\$ 67.88	1177.0	\$ 79,888.9	-	-	-	-
SBC	\$ 52.00	1967.0	\$ 102,284.0	-	-	-	-
SBC post merger	-	3144.0	\$ 182,172.9	\$ 43.87	3,360	\$ 148,400.0	-19%
Bell Atlantic	\$ 69.50	1552.8	\$ 107,918.6	-	-	-	-
GTE	\$ 77.75	1002.2	\$ 77,921.1	-	-	-	-
Verizon	-	2555.0	\$ 185,839.7	\$ 52.21	2,710	\$ 141,700.0	-24%
US West	\$ 59.19	485.0	\$ 28,703.2	-	-	-	-
Qwest	\$ 36.47	747.0	\$ 27,242.2	-	-	-	-
Qwest post merger	-	1232.0	\$ 55,945.3	\$ 23.69	1,660	\$ 40,200.0	-28%
Total RBOC			\$ 505,484.2			\$ 404,100.0	-20%

Note: US West 9/30/99 shares outstanding represents last reported shares outstanding of US West in April 1998
Source: Daily Stock Price Record, NYSE, Oct.-Dec. 1999, Standard & Poor's 2000, carriers 10Q reports

1 share, and may well drive some companies out of business or into Chapter 11 (as it did for
2 NorthPoint, Covad, Rhythms, and HarvardNet).

3

4 44. Lest there be any doubt that Wall Street's recent treatment of telecom stocks has
5 been directed specifically at CLECs rather than at the telecommunications industry as a
6 whole, RBOC shares have been performing quite respectively in light of current stock market
7 conditions. As is shown in Table 2, RBOC stocks have been fairly well insulated from the
8 recent downturn in the market, with total RBOC market capitalization declining only 20% as
9 a whole over the past 24 months. Investors and analysts thus remain far more confident that
10 Verizon and the other RBOCs will be successful in preserving their market positions and
11 associated revenue streams, which obviously would include preserving their existing
12 stranglehold over local service markets and, if provided the opportunity, the long distance
13 market as well. In fact, industry officials and financial analysts indicate that they do not
14 expect the capital markets to open up anytime soon for most cash-starved CLECs, which is
15 likely to force more CLECs to sell assets or go into bankruptcy.⁷³

16

17 45. Approval of Verizon NJ's entry into the long distance market *prior to the*
18 *development of effective, price-constraining competition in the local market* exposes
19 consumers and competitors in New Jersey to several serious risks:

20

21 73. "Facing 'Fight of Our Lives', Nation's CLECs Seek to Ramp up Support in Congress,
22 On Wall Street", *Telecommunications Reports*, December 11, 2000.

1 (1) The risk that — over and above the continued monopolization of the *local* market —
2 Verizon LD would be able to utilize its joint marketing relationship with Verizon NJ
3 to extend VNJ's local monopoly into the adjacent long distance market, thus
4 *reducing* the level of competition that presently prevails with respect to long distance
5 service.

6
7 (2) The risk that the “incentive” for Verizon to open its market to competition, currently
8 provided by the Section 271 “carrot,” will evaporate if interLATA authority is
9 obtained. Thus, the Company may “backslide,” slowing or reversing altogether the
10 market-opening measures it had pursued in order to satisfy the Section 271(c)(2)(B)
11 “Competitive Checklist,” unless the Board adopts effective self-enforcing
12 mechanisms that provide an ongoing incentive for Verizon NJ to remain in full
13 compliance with all checklist items.

14
15 (3) The result: Entry by new carriers into the New Jersey local market would be
16 discouraged, existing competitive local service providers (CLECs) would exit the
17 market, long distance carriers would also exit the market as Verizon NJ's long
18 distance market share grows, and prices for both local and long distance service
19 would inevitably increase.

20

1 **The competitive advantage available exclusively to Verizon through “joint**
2 **marketing” of local and long distance service will reduce long distance competition**
3 **and produce increased prices for long distance service for New Jersey consumers.**
4

5 46. The *source* of Verizon NJ's ability to exercise market power in the long distance
6 market *while it holds a near-monopoly in the local market* stems from its opportunity, under
7 Section 272(g) of the *Telecommunications Act of 1996*, to engage in “joint marketing” of its
8 long distance and local services. In my view, the “joint marketing” provision only implies
9 the right of a BOC and its long distance affiliate to *collaboratively* (“jointly”) participate in
10 marketing activities with respect to their respective local and long distance offerings. It does
11 not, and should not be interpreted to, permit the long distance affiliate to effectively *transfer*
12 virtually all of its long distance service sales and marketing activities to the BOC affiliate by,
13 for example, contracting for services of the affiliate's employees to perform the sales and
14 marketing functions. A BOC's ability to engage in joint marketing of its own local services
15 with its affiliate's long distance service is found in Sections 272(g)(2) and (3) of the federal
16 *Act*:

17
18 272(g)(2): BELL OPERATING COMPANY SALES OF AFFILIATE
19 SERVICES- A Bell operating company may not market or sell interLATA
20 service provided by an affiliate required by this section within any of its in-
21 region States until such company is authorized to provide interLATA services in
22 such State under section 271(d).
23

24 272(g)(3): RULE OF CONSTRUCTION- The joint marketing and sale of
25 services permitted under this subsection shall not be considered to violate the
26 nondiscrimination provisions of subsection (c).
27

1 The "nondiscrimination provisions" being referred to here are found at subsection (c)(1) of
2 Section 272:

3
4 (c) NONDISCRIMINATION SAFEGUARDS- In its dealings with its affiliate
5 described in subsection (a), a Bell operating company--
6 (1) may not discriminate between that company or affiliate and any other entity
7 in the provision or procurement of goods, services, facilities, and information, or
8 in the establishment of standards.
9

10 But subsection 272(c)(2), which is *not* superseded by subsection 272(g)(3) and thus applies to
11 joint marketing as well, states that a Bell operating company

12
13 (2) shall account for all transactions with an affiliate described in subsection
14 (a) in accordance with accounting principles designated or approved by the
15 Board.
16

17 Hence, the *Telecommunications Act* does not so much *permit* BOC joint marketing of its
18 affiliate's long distance service, but rather does not expressly prohibit it. Rather, the Act
19 merely sanctions the operation of BOCs, having satisfied the requirements of Section 271, to
20 enter into the long distance arena and to jointly market its (local) services with those of its
21 long distance affiliate, subject to all of the separate affiliate provisions set forth at Section
22 272(b), which require that VNJ's long distance affiliate:

23
24 (1) shall operate independently from the Bell operating company;
25
26 (2) shall maintain books, records, and accounts in the manner prescribed by
27 the Commission which shall be separate from the books, records, and
28 accounts maintained by the Bell operating company of which it is an
29 affiliate;
30

- 1 (3) shall have separate officers, directors, and employees from the Bell
2 operating company of which it is an affiliate;
3
4 (4) may not obtain credit under any arrangement that would permit a
5 creditor, upon default, to have recourse to the assets of the Bell
6 operating company; and
7
8 (5) shall conduct all transactions with the Bell operating company of which
9 it is an affiliate on an arm's length basis with any such transactions
10 reduced to writing and available for public inspection.
11
12 **By utilizing Verizon NJ customer service personnel to "jointly market" its long**
13 **distance services, Verizon LD is able to preempt competing IXC's by reaching**
14 **inbound customers at the time they contact Verizon NJ to order *local* service.**
15
16 47. As I shall discuss in more detail below, several FCC rulings have expanded the
17 "joint marketing" concept to expressly permit BOCs with Section 272 long distance affiliates
18 to preemptively "recommend" ("sell") their own affiliate's long distance service to *local*
19 *service* customers who contact them initially to order *local* service or for other purposes
20 related solely or primarily to matters involving *local* service. Only in those instances where
21 the "inbound" local service customer expressly asks about other long distance providers can
22 the BOC service representative then offer to read a (lengthy) list of non-affiliated
23 interexchange carriers (IXCs) that also provide such services. Experiences in both New York
24 and Texas, the first two states in which BOCs have obtained Section 271 authority, confirm
25 the extraordinary marketing advantage, *available solely to BOCs*, stemming from their use of
26 this "inbound channel", an advantage that has not been overlooked by Wall Street. Upon
27 receiving interLATA authority, Verizon NJ will be able to engage in this same type of unfair
28 use of subscriber information or unfair use of customer contacts generated by the local

1 exchange telephone company's provision of local exchange telephone service, activities that
2 conflict with the competitive checklist, and which would be harmful to competition in the
3 intrastate interLATA long distance market. As a February 8, 2001 Credit Suisse First Boston
4 ("CSFB") report commented:

5
6 We've been watching this industry for almost 20 years and we have never seen
7 consumer share gained at the rate of VZ in NY and SBC in TX (the former 20%
8 share in 12 mos and the latter 18% share in 6 months).⁷⁴
9

10 In considering whether approval of Verizon NJ's application would be in the public interest, it
11 is essential that the Board recognize that what is being sought here by Verizon is not simply
12 the right to enter yet another isolated line of business, but the right to *integrate* local and long
13 distance service into a single package, to make the two services essentially indistinguishable
14 from the consumer's perspective, and to leverage its dominance of the local market to
15 similarly come to dominate the long distance market as well. CSFB makes the point
16 profoundly clear in its comparison of (pre-merger) GTE's approach to selling long distance
17 services through a separate CLEC affiliate vs. Verizon's and SBC's ability to offer long
18 distance services directly to their ILEC customers:

19
20 In stark contrast to Verizon's huge and quick 20% consumer LD share gains in
21 NY State, LD subscribership was flat in the GTE franchise areas in '00 despite
22 GTE's benefitting from similar pre-established branding and billing relationships.
23 The difference is that GTE has not leveraged the inbound channel and also had
24 been running its LD effort through its "CLEC", in effect forcing customers to
25 switch to the GTE CLEC both their local service from GTE's ILEC and their

26 74. "VZ: Analyst Mtg Provides Comprehensive '01 Outlook," Credit Suisse First Boston,
27 09:47am EST, 8-Feb-01 ("*CSFB Report*").

1 LD service from another LD customer. Not very successful if you ask us and
2 certainly worthy of change given the empirical evidence that VZ's and SBC's
3 use of the inbound channel and separate LD sub (but not bundled with local)
4 have been extraordinarily successful.⁷⁵

5
6 48. As the CSFB report observes, this preemptive use of the "inbound channel" by both
7 Verizon and SBC to "sell" their long distance service to *new* local service customers has been
8 the principal explanation for their extraordinary success in acquiring customers in the first
9 year in which they have been permitted into the long distance business. Indeed, SBC has
10 apparently been sufficiently satisfied with its market performance that it has recently elected
11 to *increase* its interstate long distance rates in Texas. As reported in the *Ft. Worth Star-*
12 *Telegram*, February 2, 2001:

13
14 Southwestern Bell announced it was raising the interstate rate on its flagship plan
15 from 9 cents a minute to 10 cents a minute for new customers seven months after
16 entering the long-distance market in Texas. Current subscribers will see no change
17 in their domestic U.S. calling charges, said Shawn Ramsey, a San Antonio-based
18 spokeswoman for Southwestern Bell, a unit of SBC Communications.

19
20 Ramsey defended the increase, which doesn't require approval by the state's Public
21 Utility Board, by saying the plan is superior to many offered by the major long-
22 distance services. "We beat the pants off of them," she said. "We've got great rates
23 any way you slice or dice it." Asked if the higher rate reflects a need to boost
24 profits, she said: "We've been in the market about eight months now. We've learned
25 a lot and made a number of changes that reflect what we've seen. And we've
26 changed our plan accordingly."⁷⁶

27 75. *Id.*

28 76. "SW Bell raises interstate rate; current subscribers unaffected; PUC approval not
29 needed," *Ft. Worth Star-Telegram*, February 2, 2001:

1 49. Indeed, at least with respect to these types of sales at the time of the initial local
2 service contact, the BOC need spend little if any resources actually advertising or otherwise
3 marketing its long distance services. The inbound caller has already made the contact with
4 “the phone company” for basic telephone service and, unless that customer is a student of
5 telecommunications industrial organization and regulation, he or she is as likely as not to
6 accept the BOC’s “recommendation” as the only and obvious choice.

7
8 50. There is nothing “speculative” about the enormous and unique value of the sales and
9 marketing services that Verizon LD intends to purchase from Verizon NJ. The value of the
10 “inbound channel” to SBC’s long distance business in Texas has been recognized by
11 securities analysts⁷⁷ and has been graphically demonstrated by the recent moves by SBC in
12 Texas to *increase* its interLATA long distance rates.

13
14 SBC Communications, Inc., offered evidence today that increases in long
15 distance rates don’t necessarily dampen demand, especially if long distance is
16 part of a service bundle. SBC tested that theory in Oklahoma and Kansas after
17 it won FCC permission to offer interLATA services in those states, said Randall
18 Stephenson, the company’s senior vice president–finance.

19
20 “We entered Oklahoma and Kansas in the March time frame with a higher price
21 point than we entered Texas with [in July 2000], and we’re seeing penetration
22 rates very comparable to what we saw in Texas,” he said. “That product seems
23 to sustain the price increase very well.”⁷⁸
24

25 77. CSFB report, *supra*, footnote 74.

26 78. *TR Daily*, July 25, 2001.